

GIVE YOUR FAMILY A PRICELESS GIFT

Several months ago my wife and I lost a good friend who died unexpectedly. She was about our same age, active, and seemingly in good health. It was a sobering reminder that life is filled with the unexpected. Yet, from this tragic event a valuable lesson emerged about funeral planning that I'd like to share.

Our friend's husband wrote a thank you note to our church that was shared in our weekly bulletin. I have changed the names of those mentioned, but it reads in part:

"...I would, however, like to express a special thank you to Betty Benson (church staff person). Last January, Anne, as organized as she was, asked Betty to talk with us about how First Lutheran assists members in planning for funerals. I am ten years older than Anne, and she wanted us to start thinking about the future so that planning would not be done under pressure and stress.

Prior to our meeting, Anne and I talked about what we liked in funeral services, my choice of music, the spirit of services and my favorite scriptures. We found we were both comfortable with cremation. When we met with Betty in early March, we talked about places that were available in our church Columbaria, and we chose two. The first expected for me.

Shortly after Anne's death, I thanked Betty for her help and asked what more I needed to do? Betty said, "There is nothing more to do. After our meeting Anne took care of everything." I thought we were planning for my funeral, but as it turned out, the planning was a gift to me from Anne, a gift that eased stress and anxiety and gave confidence and assurance at the most difficult time of my life."

Discussing mortality with family members and loved ones is never easy, but there are helpful resources available from houses of faith and funeral homes that will assist in funeral planning. Making those plans are a lasting gift to those you love.

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THE CHIMERA OF ASSET CLASS INVESTING: “TOP QUARTILE” PERFORMANCE

In Greek mythology, a chimera was a monster that had a lion’s head, a goat’s body and serpent’s tail. In modern times, the word is synonymous with something that is wished for but is in fact impossible to achieve.

In the financial advisory world, top quartile performance is something of a chimera. Mutual fund managers have a myopic view of performance, hobbled by blinders that focus solely on their niche, peer universe or benchmark—which is understandable given the vast amounts of compensation at stake. Whether it be the result of luck or skill, an investment manager with top quartile investment performance is handsomely rewarded. We live in a Lake Wobegon world; everyone wants above average.

But what about in the real world, working with clients with differing risk tolerances, differing asset allocations and differing cash flow needs—is top quartile investment performance achievable and how might one measure it?

I recently debated this issue with a friend, Joe, who is a retired mutual fund manager. He’s a guy who refuses to accept the overwhelming evidence that argues for an asset class investment approach. His view is that a financial advisor should be measured by delivering top quartile investment performance. Let’s look at just how whimsical this idea is.

“As Nobel laureate Harry Markowitz said, “diversification is the only free lunch in finance.” I like putting my clients on the same side of the table as Nobel laureates.”

For starters, our firm espouses an investment approach that utilizes multiple equity asset classes (large cap, small cap, REITs, international and emerging markets) and we use funds from *Dimensional Fund Advisors* and *Vanguard* to build those portfolios. The allocations to those classes vary from client to client based on risk tolerance and other personal factors. As Nobel laureate Harry Markowitz said, “diversification is the only free lunch in finance.” I like putting my clients on the same side of the table as Nobel laureates.

Our investment portfolios are always comprised of five equity asset classes. Let’s assume for illustration purposes we have a client whose portfolio is 100% equity allocated as follows:

40% US LARGE
25% US SMALL CAP
15% INTERNATIONAL
15% EM
5% REITS

The first challenge is how one measures “top quartile” in this type of portfolio, one comprised of five different asset classes. On the face of it this seems very easy, but unfortunately SPIVA (an arm of Standard & Poors that measures such things) doesn’t rank such diversified portfolios. And for good reason—there is little uniformity in the asset allocations I noted above. Everyone is slightly different, based on risk tolerance, risk capacity, age, cash needs, etc.

The second challenge will be these weights shift over time, some asset classes go up while others go down. Yes, we rebalance to targets as circumstances warrant, but this makes using a static asset class index benchmark far less relevant.

We can create a “top quartile” surrogate by taking the returns of the top quartile performance for each asset class for the 15-year period ending December 31, 2017. But here’s what’s truly amazing about such a benchmark: **the chances of achieving it are about 1 in 500,000.**

Here’s why: The probability that someone can identify these exceptional managers across all five asset classes prospectively for the next 15 years is calculated by multiplying the probability of each fund outperforming its respective asset class index. **Those percentages (rounded) as of December 31, 2017 are as follows (according to SPIVA):**

LARGE CAP: 8%
SMALL CAP: 4%
INT’L: 8%
EMERGING: 5%
REITS: 19%

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When I calculate the probability of selecting funds that beat the benchmark in every asset class I get: .0002%, or about 1 in 500,000. Those aren't the odds that anyone serving their client as a fiduciary would accept, at least not this fiduciary. Instead, my job

is to create successful investment outcomes for clients, and basic math and overwhelming evidence tells me an investment strategy founded on accepting asset class returns (like DFA & Vanguard) puts the odds of investment success squarely in my favor.



HOW AN IPHONE COULD BE A FINANCIAL LIFE SAVER

We all love our smartphones. They enable us to play (music), read, work, work out and connect with others like never before. This summer I was able to FaceTime my daughter in Spain during a school trip. How cool!

Let's not forget about video. With the tap of a button we can now channel our inner Steven Spielberg and make movies. But can an iPhone be a financial life saver? Maybe. Think about losing all your worldly possessions in a fire or natural disaster. Do you have an inventory of your personal property or would you be forced to battle your insurance company to prove the replacement value of your contents?

Instead, spend 10 minutes going through your home with your iPhone recording the contents of each room. Be sure to upload the video to a cloud storage system (Dropbox, Google Docs, iCloud). Clients of our firm are encouraged to put such a video in their Client Vault. Should the unthinkable happen you have a digital record of your home's contents. If a picture paints a thousand words, then a video paints 10–20 times more.

“Do you have an inventory of your personal property or would you be forced to battle your insurance company to prove the replacement value of your contents?”





BEHIND THE SCENES

Mike Palmer's son, Brooks, recently completed a summer internship with *Dimensional Fund Advisors* in Austin, TX. Brooks will be a senior at UNC this year.

Lisa Shirley's son, Nicholas, graduated Magna Cum Laude from NC State in May with a B.S. in Mechanical Engineering. He is working with Altec Industries, Inc.

Ark Royal Wealth Management was recognized by *Financial Advisor* magazine as the top ranked NC RIA firm in the <\$100 million AUM segment.

“How could economics not be behavioral?”

CHARLIE MUNGER



The CORNERSTONES *of* ARK ROYAL WEALTH MANAGEMENT



To nurture a culture that puts our client's interest first—always



To be truthful at all times, to be intellectually honest with ourselves
and with our clients, even if it isn't what they want to hear



A commitment to lifelong learning, and a passion for applying
our wisdom efficiently and effectively every single day



Align what you say, what you do and what you think to honor
yourself, your family and our firm

